Supreme Court of the United States

OCTOBER TERM, 1942.

No. 613

LOUISVILLE GAS AND ELECTRIC COMPANY, - Petitioner,

versus

FEDERAL POWER COMMISSION, - - - Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, Louisville Gas and Electric Company, hereby petitions this Honorable Court for a writ of certiorari to be issued to review the judgment entered in the United States Circuit Court of Appeals for the Sixth Circuit on June 29, 1942 (petition for rehearing denied October 6, 1942), in the above-entitled cause and respectfully shows:

SUMMARY STATEMENT OF FACTS.

Petitioner, Louisville Gas and Electric Company (hereinafter called the Company) is a Kentucky corporation owning and operating an electric and gas business in the city of Louisville, Kentucky, and environs in Kentucky. The Company is being regulated by the Public Service Commission of Kentucky as to the rates it may charge, the service it must render, the securities it may issue, its accounts and accounting system and everything else connected with the Company. (Ky. Stats. 3952-1 to 3952-61, K. R. S. 278.010 to 278.990.) It will not be claimed by the respondent, Federal Power Commission (hereinafter called the Commission) that it has jurisdiction over the Company's rates, service or securities. The 1935 Federal Power Act, in giving the Commission jurisdiction over certain matters of certain electric companies, whether they owned licenses or not, provides that "such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States" (16 U. S. C. A. 824). The Court below held (erroneously as the Company contends) that the Commission had jurisdiction over the Company's accounts and accounting system, notwithstanding the fact that such accounts and accounting system were being regulated by the State of Kentucky.

The Company is the owner of a 50-year license granted in 1925 by the Commission for the construction and operation of a hydro-electric development at the falls of the Ohio River near Louisville, Kentucky, known as Project 289. The license was issued to Louis-

ville Hydro-Electric Company, an affiliate, and, with the Commission's consent, was transferred to the Company. The license was issued pursuant to the Federal Water Power Act of 1920 (41 Stat. 1077, 16 U. S. C. A. 791-823).

This 1920 Act gave the Commission jurisdiction over the rates, service, securities, etc., of all licensees. However, to preserve State regulation of local or intrastate matters, and to avoid the unthinkable effects of dual control the 1920 Act provided that "the jurisdiction of the Commission shall cease and determine as to each specific matter of regulation and control prescribed in this section as soon as the State shall have provided a commission or other authority for the regulation and control of that specific matter" (16 U. S. C. A. 812).

The 1920 Act also gave the Commission jurisdiction to prescribe a system of accounts for licensees (16 U. S. C. A. 797f). However, the Commission to preserve State regulation of local matters and to avoid unworkable dual control provided in its first System of Accounts dated November 20, 1922, that where "the records and accounts of such licensee are kept and maintained under and in conformity with the accounting rules and regulations prescribed by the public utility commission or other commission or regulatory body of the State or States in which the project is located, the licensee will not be required to maintain also the system of accounts provided by Section 1 hereof, but the system of accounts prescribed by the State regulatory body may be substituted therefor if desired." Thus, under

the 1920 Act, both Congress and the Commission expressly refrained from Federal regulation of matters that were being regulated by the States. This policy of non-interference with matters that were being regulated by the States was sealed into the law in the Federal Power Act of 1935, as a limitation on the Commission's powers of regulation as follows: "* * * such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States" (59 Stat. 847, 16 U. S. C. A., Sec. 791).

That part of the 1920 Act (16 U. S. C. A. 797 (f)) which gave the Commission jurisdiction over the accounts and accounting system of licensees was repealed by the 1935 Federal Power Act, so that the Commission since 1935 has no more jurisdiction over the accounts and accounting system of a licensee than of other electric utility companies.

Under the 1920 Act, the Commission was directed to make a "determination" of the "net investment" of every licensed project on completion of the project (16 U. S. C. A. 797). "Net investment" is defined in the 1920 Act to mean the "actual legitimate original cost" as defined and interpreted in the Classification of Investment in Road and Equipment of Steam Roads, issue of 1914, Interstate Commerce Commission plus similar costs of additions thereto minus the sum of several items. Thus, "actual legitimate original cost" is one of the factors to be determined in arriving at the "net investment" of a licensed project. There is nothing occult or mysterious about the words "actual legitimate original cost." They are not contained

in the I. C. C. 1914 classification, nor are they contained in any other classification or system of accounts. An examination of the 1914 I. C. C. classification shows that the words mean nothing more or less than original cost.

Jurisdiction to determine the "net investment" or "actual legitimate original cost" of a licensed project was not for the purpose of regulating rates, services or securities because the 1920 Act gave the Commission jurisdiction over these matters only in those cases where there was no State regulatory body with jurisdiction. Nor was it for the purpose of regulating the licensees' system of accounts because the Commission disclaimed jurisdiction over a licensees' system of accounts where the licensee was following a State Commission's system of accounts. Jurisdiction to determine "net investment" or "actual legitimate original cost" of a licensed project was for three purposes only:

(a) Amortization reserves after the first 20 years of operation (16 U. S. C. A. 803-d). Project 289 was put into operation in 1928 so the Commission's "finding" of "net investment" could not be used for this purpose until 1948.

(b) Recapture or purchase by the Government. The 1920 Act provided (16 U. S. C. A., Sec. 807) that the United States has the right to recapture or purchase a licensed project at the expiration of the license, and that the Government should pay the "net investment" to be "determined by agreement between the Commission and the licensee, and in case they cannot agree by proceedings in equity instituted by the United

States." This section was amended by the Federal Power Act of 1935 to provide that if the parties could not agree on the "net investment," then it should be "determined by the Commission after notice and opportunity for hearing." So that in no instance was the Commission's "determination" of the "net investment" or "actual legitimate original cost," made on completion of a project, final and binding. Under the 1920 Act, if the Government decided to purchase, the "net investment" was to be fixed by agreement or by the Court at the time of the purchase. Under the 1935 Act, it is to be fixed by agreement at the time of the purchase or determined by the Commission at that time "after notice and opportunity for hearing" from which there could be an appeal to the Courts. The license for Project 289 was issued in 1925, and was for 50 years so that the time for using "net investment" for a recapture or purchase by the Government will not arise until 1975.

(c) The other provision of the 1920 Act where the finding of "net investment" by the Commission might be pertinent would be in the event of an emergency taking over of the project by the Government, in which event the Government is required to pay "just and fair compensation for the property" (16 U. S. C. A., Sec. 809). "Net investment" might be evidence on the question of compensation.

The 1920 Act provided (16 U. S. C. A. 797 (a)) that in order to aid the Commission in determining the "net investment" the licensee after the construction of the original project or any addition thereto shall

file a verified statement showing the "actual legitimate original cost" of construction of the project. Such a statement was filed for Project 289. The Commission's Staff made an investigation and filed a Preliminary Accounting Report, taking exception to certain items. After a hearing the Commission rendered Opinion No. 11 on October 31, 1933 (R., Vol. II, p. 963). On that same date it entered an order styled "Order Determining Cost of Project 289, Ky. (Ohio Falls)" (R., Vol. II, p. 1000). By this order the Commission determined that the "actual legitimate original cost" of Project 289 was some $800,000 less than had been claimed in the statement and expended on the project. In response to a petition for rehearing there was an additional hearing, and on September 30, 1937, the Commission entered another order styled "Determination of Actual Legitimate Cost" (R., Vol. II, p. 1256). This order allowed approximately $200,000 that had been disallowed in the 1933 order. The net result of the two orders was a disallowance of $601,-973.57 that had actually been spent in the construction of the project.

There is nothing in the 1933 or 1937 orders, which were mere "determinations" or "findings" of cost, remotely suggesting that the Commission had in mind any idea that the disallowed amount should be charged to surplus. The orders did not direct the Company to do anything except make a mere bookkeeping entry showing the Commission's "determination" of the "actual legitimate original cost" of Project 289. The Company believed that the orders were erroneous in making the

disallowances, but was willing to and did make the bookkeeping entries. In fact, it was necessary under the law for the Commission to make a "determination" of "net investment" or "actual legitimate original cost," and it was proper for such "determination" to be recorded in the Company's books as a memorial of the Commission's finding, such determination to be used subsequently as to amortization reserves, recapture, emergency taking over or any other matter as to which the Commission might have jurisdiction over the Company and if so subsequently used to the detriment of the Company there would be the right of appeal to the Court.

Although the Commission had made numerous "determinations" of the "actual legitimate original cost" of licensed projects, the Commission never in any instance, prior to 1939, intimated that the disallowed amount should be charged to surplus. It was shown in the Company's petition for rehearing in the Court below (R., Vol. III, p. 1489) that from at least 1920 to the present, the Company's books, records and accounts are annually audited by a national firm of certified public accountants. This firm was furnished a copy of the 1933 Order and a copy of the 1937 Order when the audits were made for those years. These independent accountants did not think that either of the Orders required or even intimated that the disallowed amount should be charged to surplus. If they had thought anything of the kind, they would obviously have so stated in their annual audit and report for these and subsequent years until the matter was settled.

Clearly they would not have failed to note the possibility of the Company losing such a large amount of its surplus, and yet the independent auditors never made any mention of either the 1933 or 1937 orders. The 1939 and subsequent audits have referred to a 1939 Order of the Commission referred to hereafter.

The Company is required to register new or refunding securities with the Securities and Exchange Commission. It was shown to the Court below (R., Vol. III, p. 1494) that in 1936 the Company issued and sold $28,000,000 "First and Refunding Mortgage Bonds 3½% Series due 1966." The Securities and Exchange Commission has a form for the registration of securities which requires a full disclosure of everything concerning the applicant company. The law provides heavy penalties against the applicant company, its officers and directors for the misstatement of a material fact or for the omission to state a material fact. As a part of such registration statement, applicants are required to file audits and statements by independent certified public accountants. It stands to reason that if the Company its officers and directors or if the underwriters or the independent accountants or any of the above had had even a mere suspicion that the 1933 Order involved the possibility, however remote, of so large a charge to surplus they would not have dared to omit to state such a material fact. The fact that the 1936 Registration Statement of this Company contained no hint that the Commission's Order of 1933 involved the possibility of a charge to surplus is a demonstration that each and all of the parties to that regis-

tration statement thought that the Order involved a mere bookkeeping entry only.

The then Commission and its then staff were likewise of this opinion. The Commission's brief, involving an order identical with our 1933 and 1937 orders, filed November 3, 1933,[1] contained formal, full agreement by the Commission with our contention that the 1933 and 1937 Orders were not appealable until subsequently used to the Company's detriment as follows:

> p. 12. "The concurring opinion of Commissioner McNinch (12th Annual Report, Federal Power Commission, page 217) refers to the argument presented by the plaintiff before the Commission in which plaintiff contended that if the Commission possesses the power to determine currently the cost of licensee's project such determination 'could not be reviewed earlier than 20 years and perhaps not until the expiration of the license period, 50 years, * * *' The defendants are in full agreement with the position thus taken by plaintiff's counsel at that time that there can be no judicial review of the Commission's cost determination order until occasion arises when the Commission shall undertake to use such determination, in an amortization, or recapture, or similar proceeding."

More than a year and a half after the Order of September, 1937, like a "bolt out of the clear," the Commission on April 4, 1939, issued an order styled, "Order to Show Cause" (R., Vol. II, p. 1270), in which

[1]In the case of Alabama Power Company v. Smith and others as members of the Federal Power Commission in the Court of Appeals for the District of Columbia on the Commission's motion to dismiss.

it directed the Company to show cause under oath why the disallowed amount of $601,973.57 should not be charged to the Company's surplus account. Under Kentucky law, a corporation's surplus is property which may be used for any legitimate corporation purpose (*Smith* v. *Southern Foundry Company,* 166 Ky. 208, 179 S. W. 205). This is also general law. The consent of the Securities and Exchange Commission is not necessary for the payment of dividends out of earned surplus. That Commission has frequently authorized the payment of dividends out of unearned surplus. All of the Company's surplus has been earned in the hard way and set aside for future emergencies. It is not known what would have happened to the Company after the 1937 disastrous Ohio River flood, except for the surplus that it had accumulated. A charge of $601,973.57 to surplus is no mere bookkeeping entry. It would wipe out more than half of the Company's surplus. It would take the Company's property just as effectively as if the Company were required to pay $601,973.57 to some third party. During all of the 19 years that the 1920 Act had been in effect, the Commission had never until that time attempted to direct that the disallowed amount in a "determination" of "actual legitimate original cost" of a licensed project should be charged to surplus.

The Company filed a response to the Show Cause Order (R., Vol. II, p. 1279). Without any hearing or opportunity to be heard, the Commission on October 31, 1939, entered an order directing the Company to charge the disallowed amount of $601,973.57 to sur-

plus. The Company filed a petition for rehearing (R., Vol. 2, p. 1275). The response and the petition for rehearing contended among other things, (a) that the Commission had no jurisdiction over the Company's accounts and accounting system; (b) that the 1933 and the 1937 Orders did not contain any notice of a proposed charge to surplus; (c) that the orders, rules, regulations and system of accounts of the Public Service Commission of Kentucky required that the $601,973.57 should be kept in the Company's Electric Plant account, and not charged to surplus. The petition for rehearing also contended that the 1939 Order was entered without notice or hearing. When the petition for rehearing was not acted upon within 30 days the Company was required to take it as having been denied (16 U. S. C. A. 825 (l)), and filed its petition in the Sixth Circuit Court of Appeals for a review and the setting aside of the 1933, 1937 and 1939 Orders. The petition for review is printed in Vol. 3 of the Record beginning at p. 1337. The petition for review made the same contentions that were made before the Commission.

The Sixth Circuit Court of Appeals (a) held that the Commission had jurisdiction over the Company's accounts and accounting system, (b) sustained the Commission's motion to dismiss the petition for review insofar as it applied to the 1933 and 1937 orders and (c) affirmed the Commission's 1939 order. The reason for dismissing the appeal as to the 1933 and 1937 orders was stated by the Court below to be because in the Court's opinion the 1933 and 1937 orders

required that the disallowed amount be charged to surplus, that the Company should have known this, and that therefore appeals should have been, but were not taken within the time provided by Section 313 (a) and (b) of the Federal Power Act of 1935. Of course, when the 1933 order was entered the 1935 Federal Power Act had not been passed and under the 1920 Act there was no limit as to when appeals could be taken. The petition for rehearing showed to the Court below that the then Commission and its then Staff were contending in other cases as we are contending, *i. e.,* that orders similar to our 1933 and 1937 orders would not harm or hurt the licensee and were therefore not appealable unless and until they were subsequently used to the detriment of the licensee. Due to a change in personnel and a resultant change in policy of the Commission, this Company has been caught in what this Court through Mr. Justice Holmes has politely called, "between Scylla and Charybdis" (*Cedar Rapids Gas Company* v. *Cedar Rapids,* 223 U. S. 655.

STATEMENT OF JURISDICTION.

The jurisdiction of this Court is invoked under Section 313 (b) of the Federal Power Act (49 Stat. 860, 16 U. S. C. A., Sec. 825 l) and Section 240 of the judicial code as amended (43 Stat. 938, Sec. I, 28 U. S. C. A., Sec. 347). The Statutes, the validity of which are involved is the the 1935 Federal Power Act (49 Stat. 847, 16 U. S. C. A., Sec. 791 (a)) and the Federal Water Power Act of 1920 (41 Stat. 1077, 16 U. S. C. A. 791-823). The judgment of the Circuit Court of Ap-

peals was entered June 29, 1942, and petition for rehearing was denied October 6, 1942, and this petition is filed within three months thereafter.

QUESTIONS PRESENTED.

(1) Whether the Commission has jurisdiction over the Company's accounts and accounting system.

The Public Service Commission of Kentucky has and is exercising complete jurisdiction over the accounts and accounting system not only but also over the rates service, securities, etc., of the Company. The jurisdiction of the Federal Commission is thus limited by the 1935 Federal Power Act: "* * * such Federal regulation however to extend only to those matters which are not subject to regulation by the States." If this Court agrees with us on this question it would be an end of the case.

(2) Whether the Company is to be denied a judicial review of the Commission's 1933 and 1937 "determinations" of "actual legitimate original cost" because the Company thought as the then Commission and its then staff thought, *i. e.*, that such orders did not adversely affect it, and that no appeal could be taken unless and until such orders were subsequently used to the Company's detriment on the question of amortization, repurchase or other matters as to which the Commission had jurisdiction.

(3) Whether the Commission could make the 1939 order directing a charge of $601,973.57 to surplus without giving the Company any hearing thereon.

REASONS FOR GRANTING THE WRIT.

(1) The decision of the Circuit Court of Appeals involves a question of Federal law which has not been, but should be settled by this Court.

Does the Commission have jurisdiction over the Company's accounts and accounting system when the 1935 Federal Power Act limits the jurisdiction of the Commission to "those matters which are not subject to regulation by the States," and when the Company's accounts and accounting system rates, service, securities, etc., are being regulated by the Public Service Commission of Kentucky.

This question of Federal Law is important not only to the Company, but to a very large number of other electric companies. It should be decided by this Court.

(2) The decision of the Circuit Court of Appeals dismissing the appeal as to the 1933 and 1937 orders is in conflict with the decision of this Court that an order of a regulatory body making a "finding" of value or cost is not appealable unless and until it is used subsequently to the Company's disadvantage *United States* v. *Los Angeles R. R. Co.*, 273 U. S. 299. Since this was also the opinion of the then Commission, a change of personnel and of policy should not be used to squeeze the Company "between Scylla and Charybdis."

The decision is also in conflict with decisions of this Court that orders of a regulatory body which do not harm or adversely effect a party can not be appealed to the Courts *Rochester Telephone Corpora-*

tion v. *United States, et al.*, 307 U. S. 125; *Federal Power Commission* v. *Pacific Power & Light Co.*, 307 U. S. 159.

CONCLUSION.

For the reason herein set forth, it is respectfully submitted that this petition should be granted.

Respectfully submitted,

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